

**ALPINE BANKS OF COLORADO  
AND SUBSIDIARIES**

CONSOLIDATED FINANCIAL STATEMENTS  
AND  
INDEPENDENT AUDITOR'S REPORT

December 31, 2019 and 2018



**Alpine Banks  
of Colorado**



DALBY, WENDLAND & CO., P.C.  
*CPAs and Business Advisors*



DALBY, WENDLAND & CO., P.C.

Grand Junction

*CPAs and Business Advisors*

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Board of Directors  
Alpine Banks of Colorado and Subsidiaries  
Glenwood Springs, Colorado

## **INDEPENDENT AUDITOR'S REPORT**

We have audited the accompanying consolidated financial statements of Alpine Banks of Colorado and Subsidiaries (the Bank), which comprise the consolidated statements of financial condition as of December 31, 2019 and 2018, and the related consolidated statements of comprehensive income, changes in stockholders' equity, and cash flows for the years then ended, and the related notes to the consolidated financial statements.

### **Management's Responsibility for the Consolidated Financial Statements**

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

### **Auditor's Responsibility**

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

### **Opinion**

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Alpine Banks of Colorado and Subsidiaries as of December 31, 2019 and 2018, and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

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**Report on Internal Control Over Financial Reporting**

We also have audited in accordance with auditing standards generally accepted in the United States of America, Alpine Banks of Colorado and Subsidiaries' internal control over financial reporting as of December 31, 2019, based upon the criteria established in the *2013 Internal Control – Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission and our report dated February 1, 2020 expressed an unmodified opinion.

A handwritten signature in blue ink that reads "Dalby Wendland & Co. P.C." in a cursive script.

DALBY, WENDLAND & CO., P.C.  
Grand Junction, Colorado

February 1, 2020

**ALPINE BANKS OF COLORADO  
AND SUBSIDIARIES**

CONSOLIDATED STATEMENTS OF FINANCIAL CONDITION

December 31, 2019 and 2018

(In thousands, except share amounts)

	2019	2018
<b>ASSETS</b>		
Cash and due from banks	\$ 313,443	\$ 367,751
Investment securities:		
Securities available for sale, at fair value	129,731	186,313
Securities held to maturity, at amortized cost	541,783	547,661
Investments in Alpine Capital and trust preferred securities	2,091	2,091
Loans receivable, net of allowance for loan losses and deferred loan fees	2,640,826	2,401,637
Loans held for resale, at cost which approximates fair value	14,999	5,253
Accrued interest receivable	11,420	11,712
Cash surrender value of life insurance policies	68,741	66,135
Bank property, equipment, and leasehold improvements, net	72,535	74,549
Goodwill	17,631	17,631
Deferred tax asset, net	8,814	11,646
Other assets	43,148	17,908
<i>Total Assets</i>	\$ 3,865,162	\$ 3,710,287
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
<b>Deposits</b>		
Demand	\$ 1,249,129	\$ 1,169,932
Interest Checking	758,938	759,487
Money Fund	1,093,616	1,065,221
Savings	121,250	128,262
Certificates of deposit	138,517	152,277
Repurchase agreements	37,071	39,067
<i>Total Deposits</i>	3,398,521	3,314,246
<b>Other Liabilities</b>		
Other liabilities	54,141	29,041
Accrued interest payable	430	454
Subordinated debentures	69,179	69,179
<i>Total Other Liabilities</i>	123,750	98,674
<i>Total Liabilities</i>	3,522,271	3,412,920
<b>Equity</b>		
Alpine Banks of Colorado Stockholders' equity		
Common stock, Class A, voting no par value, 100,000 shares authorized, 53,043 (2019) and 53,440 (2018) shares issued and outstanding	26	26
Common stock, Class B, non-voting no par value, 100,000 shares authorized, 51,631 (2019) and 51,697 (2018) shares issued and outstanding	26	26
Contributed capital	8,668	11,225
Retained earnings	333,536	289,089
Accumulated other comprehensive income (loss), net of tax effect	186	(3,509)
<i>Total Alpine Banks of Colorado Stockholders' Equity</i>	342,442	296,857
Noncontrolling interest	449	510
<i>Total Equity</i>	342,891	297,367
<b><i>Total Liabilities and Stockholders' Equity</i></b>	<b>\$ 3,865,162</b>	<b>\$ 3,710,287</b>

See accompanying notes.

**ALPINE BANKS OF COLORADO  
AND SUBSIDIARIES**

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

For the years ended December 31, 2019 and 2018

(In thousands, except per share amounts)

	2019	2018
<b>Interest Income</b>		
Loans receivable	\$ 143,326	\$ 128,052
Securities	27,462	26,431
<i>Total Interest Income</i>	170,788	154,483
<b>Interest Expense</b>		
Deposits	4,859	3,238
Other	4,755	4,604
<i>Total Interest Expense</i>	9,614	7,842
<i>Net Interest Income</i>	161,174	146,641
<b>Non-interest Income</b>		
Other income	25,081	22,730
Service charges on deposit accounts	10,159	9,353
Earnings on life insurance	1,455	1,605
<i>Total Non-interest Income</i>	36,695	33,688
<b>Non-interest Expense</b>		
Salaries and employee benefits	72,598	65,261
Other expense	37,074	31,762
Occupancy expense	7,823	6,767
Furniture and fixture expense	10,034	9,569
<i>Total Non-interest Expense</i>	127,529	113,359
<i>Net Income Before Income Taxes</i>	70,340	66,970
<b>Income Tax Expense</b>	12,332	12,119
<i>Net Income</i>	58,008	54,851
Less: Net loss attributed to noncontrolling interest	(13)	(3)
<i>Net Income Attributed to Alpine Banks of Colorado and Subsidiaries</i>	58,021	54,854
<b>Other Comprehensive Income (Loss), Net of Tax</b>		
Change in unrealized gain (loss) on investment securities, net of reclassification adjustment and tax effects	3,695	(1,419)
<i>Comprehensive Income Attributed to Alpine Bank and Subsidiaries</i>	\$ 61,716	\$ 53,435
Basic earnings per common share	\$ 553	\$ 520
Dividends per common share	\$ 116	\$ 108

See accompanying notes.

**ALPINE BANKS OF COLORADO  
AND SUBSIDIARIES**  
CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY

For the years ended December 31, 2019 and 2018  
(In thousands)

	Class A Common Stock	Class B Common Stock	Contributed Capital	Retained Earnings	Other Comprehensive Income	Noncontrolling Interest	Total Equity
<b>Balance at December 31, 2017</b>	\$ 26	\$ 26	\$ 14,705	\$ 245,277	\$ (1,720)	\$ 591	\$ 258,905
Net income (loss)	-	-	-	54,854	-	(3)	54,851
Change in unrealized gain (loss) on securities, net of reclassification adjustment and tax effects	-	-	-	-	(1,419)	-	(1,419)
Reclassification of accumulated other comprehensive income due to tax rate change	-	-	-	370	(370)	-	-
Capital contribution - noncontrolling interest	-	-	-	-	-	92	92
Capital stock retirement	-	-	(3,480)	-	-	-	(3,480)
Distributions - noncontrolling interest	-	-	-	-	-	(170)	(170)
Dividends paid	-	-	-	-	-	-	-
Common stock	-	-	-	(11,412)	-	-	(11,412)
<b>Balance at December 31, 2018</b>	26	26	11,225	289,089	(3,509)	510	297,367
Net income (loss)	-	-	-	58,021	-	(13)	58,008
Change in unrealized gain (loss) on securities, net of reclassification adjustment and tax effects	-	-	-	-	3,695	-	3,695
Reclassification of accumulated other comprehensive income to retained earnings upon adoption of ASU 2016-1	-	-	-	(1,292)	-	-	(1,292)
Capital contributions - noncontrolling interest	-	-	-	-	-	127	127
Capital stock retirement	-	-	(2,557)	-	-	-	(2,557)
Distributions - noncontrolling interest	-	-	-	-	-	(175)	(175)
Dividends paid	-	-	-	-	-	-	-
Common stock	-	-	-	(12,282)	-	-	(12,282)
<b>Balance at December 31, 2019</b>	<b>\$ 26</b>	<b>\$ 26</b>	<b>\$ 8,668</b>	<b>\$ 333,536</b>	<b>\$ 186</b>	<b>\$ 449</b>	<b>\$ 342,891</b>

See accompanying notes.

**ALPINE BANKS OF COLORADO  
AND SUBSIDIARIES**

CONSOLIDATED STATEMENTS OF CASH FLOWS

For the years ended December 31, 2019 and 2018  
(In thousands)

	2019	2018
<b>Cash Flows From Operating Activities</b>		
Net income	\$ 58,021	\$ 54,854
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation expense	8,595	7,078
Write-down of other real estate owned	622	-
Amortization of premiums and accretion of discounts	290	1,137
Gain on sale of other real estate owned	(20)	(162)
Gain on sale of assets	(805)	(30)
Proceeds from loan sales	218,434	258,034
Loans originated for resale	(228,180)	(253,977)
Change in cash surrender value of life insurance policies	(1,310)	(1,615)
Changes in operating assets and liabilities:		
Accrued interest receivable	292	(794)
Deferred tax asset, net	2,832	737
Other assets	(27,706)	(4,906)
Other liabilities	25,100	(1,101)
Accrued interest payable	(24)	40
Minority interest of limited liability companies	(61)	(81)
<i>Net Cash Provided by Operating Activities</i>	<b>56,080</b>	<b>59,214</b>
<b>Cash Flows From Investing Activities</b>		
Maturities of investment securities available for sale	104,524	10,410
Maturities of investment securities held to maturity	91,349	31,482
Purchases of investment securities available for sale	(44,010)	(52,637)
Purchases of investment securities held to maturity	(85,671)	(42,643)
Net increase in loans made to customers	(239,097)	(166,587)
Proceeds from sale of other real estate owned	153	2,191
Proceeds from sale of equipment and other assets	4,142	144
Purchase of Bank property and equipment	(9,918)	(10,270)
Premiums paid on life insurance policies	(4,000)	(4,000)
Cash received on life insurance policies released	2,704	-
<i>Net Cash Used by Investing Activities</i>	<b>(179,824)</b>	<b>(231,910)</b>
<b>Cash Flows From Financing Activities</b>		
Net increase in deposits	84,275	192,891
Payments on other borrowed funds	-	(97)
Dividends paid:		
Common stock	(12,282)	(11,412)
Capital stock retirement	(2,557)	(3,480)
<i>Net Cash Provided by Financing Activities</i>	<b>69,436</b>	<b>177,902</b>
<i>Net Increase (Decrease) in Cash and Due From Banks</i>	<b>(54,308)</b>	<b>5,206</b>
<b>Cash and Due From Banks - beginning of the year</b>	<b>367,751</b>	<b>362,545</b>
<b>Cash and Due From Banks - end of the year</b>	<b>\$ 313,443</b>	<b>\$ 367,751</b>
<b>Supplemental Disclosures:</b>		
Cash paid during the year for interest	<b>\$ 9,638</b>	<b>\$ 7,802</b>
Cash paid during the year for income taxes	<b>\$ 9,572</b>	<b>\$ 15,192</b>
Transfers from loans to other real estate owned	<b>\$ 92</b>	<b>\$ 57</b>

See accompanying notes.

**ALPINE BANKS OF COLORADO  
AND SUBSIDIARIES**  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
December 31, 2019 and 2018

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**NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

**Nature of Operations**

Alpine Banks of Colorado and Subsidiaries (the Bank), through its wholly-owned subsidiary, provides a variety of banking services to individuals and businesses at forty locations primarily on the western slope of Colorado. Its primary deposit products are demand deposits and certificates of deposit, and its primary lending products are commercial business, real estate mortgage, and installment loans. The Bank also owns real estate, which consists primarily of commercial buildings.

**Consolidation**

The consolidated financial statements include the accounts of the Bank and its wholly-owned subsidiary, Alpine Bank (Alpine). Alpine has investments in four limited liability companies (LLCs) as follows: ENIPLA Building, LLC (99%); Check Clearing House Aviation, LLC (80%); Alpine Avon Building Company, LLC (99%); and I-70 Business Center, LLC (33%). All material intercompany transactions have been eliminated in consolidation.

The Bank evaluates variable interest entities in which it holds a beneficial interest for consolidation. Variable interest entities are legal entities with insubstantial equity, whose equity investors lack the ability to make decisions about the entity's activities, or whose equity investors do not have the right to receive the residual returns of the entity if they occur. I-70 Business Center, LLC is considered to be a variable interest entity of the Bank and therefore is consolidated with the Bank.

**Segment Reporting**

The Bank is managed as a single entity and not by departments or lines of business. Based on management's analysis, no department or line of business meets the criteria established in Accounting Standards Codification 280, Segment Reporting, for reporting of selected information about operating segments.

**Use of Estimates**

The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Material estimates that are particularly susceptible to significant change in the near term relate to the determination of the allowance for loan losses and the valuation of deferred tax assets.

**Cash and Due from Banks**

For purposes of the consolidated statements of cash flows, cash and cash equivalents include cash and amounts due from banks, which mature within three months at the date of purchase. At various times, cash and due from bank balances could exceed federally insured limits.

**Investment Securities**

The Bank's investment securities are classified in two categories and accounted for as follows:

Securities Available for Sale. Bonds, notes, debentures, mutual funds and certain equity securities are classified as available for sale when they might be sold before maturity. These securities are carried at fair value, with any unrealized gains and losses, net of tax, reported as a component of other comprehensive income. Gains and losses on the sale of securities available for sale are determined using the specific-identification method.

Securities Held to Maturity. Bonds, notes, and debentures are classified as held to maturity when the Bank has the positive intent and ability to hold to maturity. These securities are carried at cost, and adjusted for the amortization of premiums and accretion of discounts. Premiums are recognized in interest income using the interest method over the period to the first call date for callable securities and to maturity for non-callable securities. Discounts are recognized in interest income using the interest method over the period to maturity.

### **Federal Home Loan Bank**

The Bank is a member of the Federal Home Loan Bank of Topeka (FHLB). Membership requires the Bank to maintain a minimum investment in FHLB capital stock. The minimum investment is determined by the FHLB board of directors based on their own regulatory capital requirements. The FHLB stock is a restricted security investment, carried at cost, and evaluated for impairment.

### **Loans Receivable**

Loans receivable, that management has the intent and ability to hold for the foreseeable future or until maturity or payoff, are reported at their outstanding unpaid principal balances adjusted for any charge-offs, allowance for loan losses, any deferred fees or costs on originated loans, and unamortized premiums or discounts on purchased loans.

Loan origination fees, net of certain direct origination costs, are deferred and recognized as an adjustment of the related loan yield.

Generally, the Bank places loans on nonaccrual status if the deterioration in the financial condition of the borrower renders collection of principal and interest unlikely, if payment in full of principal and interest is not expected, or if the loans have been in default for 90 days or more, unless it is both well secured and in the process of collection. Loans are returned to accrual status when none of their principal and interest are due or unpaid or when they otherwise become well secured and in the process of collection. When interest accrual is discontinued, all unpaid accrued interest is reversed. Interest income is subsequently recognized only to the extent cash payments are received.

A loan is considered impaired when, based on current information and events, it is probable that the Bank will be unable to collect the scheduled principal and interest when due, according to the contractual terms of the loan agreement. Factors considered by management in determining impairment include payment status, collateral value, and the probability of collecting scheduled principal and interest payments when due. Loans that experience insignificant payment delays and payment shortfalls generally are not classified as impaired. Management determines the significance of payment delays and payment shortfalls on a case-by-case basis, taking into consideration all the circumstances surrounding the loans the borrower, including the length of the delay, the reasons for the delay, the borrower's prior payment record, and the amount of the shortfall in relation to the principal and interest owed.

A loan is charged off as soon as it becomes evident that there is no longer a reasonable chance of repayment. Any unsecured loan or unsecured portion of a loan which is more than 120 days past due is charged off unless repayment is imminent. Loans in nonaccrual status at year end were \$2,653,000 (2019) and \$5,410,000 (2018), and the total recorded investment in loans past due 90 days or more and still accruing interest was \$56,000 (2019) and \$0 (2018).

In situations where, for economic or legal reasons related to a borrower's financial difficulties, the Bank grants a concession for other than an insignificant period of time to the borrower that they would otherwise consider, the related loan is classified as Troubled Debt Restructuring (TDR). These modified terms may include rate reductions, principal forgiveness, term extensions, payment forbearance and other actions intended to minimize our economic loss and to avoid foreclosure or repossession of the collateral, if applicable. For modifications where the Bank forgives principal, the entire amount of such principal forgiveness is immediately charged off. Loans classified at TDRs, are considered impaired loans.

### **Allowance for Loan Losses**

The allowance for loan losses reflects management's judgment as to the level considered appropriate to absorb inherent credit losses in the loan portfolio. This judgment is based on the size and current risk characteristics of the portfolio, a review of individual loans, along with historical and anticipated loss experience. External influences such as general economic conditions, economic conditions in the relevant geographic areas and specific industries, regulatory guidelines, and other factors are also assessed in determining the level of allowance.

The allowance is determined subjectively, requiring significant estimates, including the timing and amount of expected future cash flows on impaired loans, consideration of current economic conditions, and historical loss experience pertaining to pools of homogeneous loans, all of which may be susceptible to change. The allowance is adjusted through a provision that is charged to earnings, based on management's periodic evaluation of the factors previously mentioned, and is reduced by charge-offs, net of recoveries.

The Bank has established a formal process for determining an adequate allowance that has two components. The components of the allowance estimates were developed pursuant to the Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) 450-10 and FASB ASC 310-10.

The FASB ASC 450-10 component represents the estimated probability, undetected losses inherent within the portfolio due to uncertainties in economic conditions, delays in obtaining information about a borrower's financial condition, delinquent loans that have not been determined to be impaired, trends in speculative real estate construction lending, results of internal and external loan reviews, and other factors. This component of the allowance is calculated by assigning a certain risk weighting to each identified risk factor.

To determine the FASB ASC 310-10 component, management determines loans that are impaired. For loans that are impaired, an allowance is established when the discounted cash flows (or collateral value or observable market value) of the impaired loan is lower than the carry value of that loan.

### **Loans Held for Sale**

Mortgage loans originated and intended for sale in the secondary market are carried at fair value. Loans held for sale are fixed and variable rate single-family residential mortgage loans under contract to be sold in the secondary market. In most cases, loans in this category are sold within thirty days. These are sold with the mortgage servicing rights released. During the year ended December 31, sales of mortgage loans held for sale were \$218,434,000 (2019) and \$258,034,000 (2018).

The Bank enters into commitments to originate loans whereby the interest rate on the prospective loans is determined prior to funding (rate lock commitments). Rate lock commitments on mortgage loans that are intended to be sold are considered to be derivatives. Accordingly, such commitments, along with any related fees received from potential borrowers, are recorded at fair value as derivative assets or liabilities, with the changes in fair value recorded in other income and expense. See Derivative Financial Instruments below for additional information.

### **Bank Property, Equipment, and Leasehold Improvements**

Bank property, equipment, and leasehold improvements are stated at cost less accumulated depreciation. Depreciation is computed using the straight-line method over the estimated useful lives of the assets.

### **Leases**

On January 1, 2019, the Bank adopted FASB ASC 842, *Leases* (FASB ASC 842). FASB ASC 842 requires substantially all leases to be recognized by lessees on their balance sheets as a right-of-use (“ROU”) asset and a corresponding lease liability, but recognize expenses in their income statements in a manner similar to current practice. The Bank enters into non-cancelable operating lease agreements related to certain banking offices and back-office operational facilities. The Bank does not have leases designated as finance leases. The Bank determines if an arrangement is a lease at inception. Operating lease ROU assets and liabilities are included in Bank property, equipment, and leasehold improvements, net and other liabilities on the consolidated statements of financial condition. ROU assets represent the right to use an underlying asset for the lease term and lease liabilities represent the obligation to make lease payments arising from the lease. Operating lease ROU assets and lease liabilities are recognized at commencement date based on the present value of lease payments over the lease term. As the Bank’s leases do not provide an implicit rate, the Bank uses the FHLB of Topeka’s term advance borrowing rates based on the information available at commencement date in determining the present value of lease payments. The Bank’s lease terms may include options to extend or terminate the lease when it is reasonably certain that the Bank will exercise that option. Lease expense for the lease payments is recognized on a straight-line basis over the lease term (see Note 5).

### **Impairment of Long-Lived Assets**

FASB ASC 360-10 establishes accounting standards for determining and measuring impairment of certain long-lived assets. Under provisions of FASB ASC 360-10, impairment losses are recognized when expected future cash flows are less than the asset’s carrying value. No long-lived assets were considered impaired as of December 31, 2019 and 2018.

### **Goodwill**

Goodwill is recorded in business combinations under the purchase method of accounting when the purchase price is higher than the fair value of net assets, including identifiable intangible assets. Goodwill is assessed for impairment annually, and more frequently in certain circumstances. Impairment exists when the carrying amount of the goodwill exceeds its implied fair value. The Bank recognizes impairment losses as a charge to noninterest expense and an adjustment to the carrying value of the goodwill asset (see Note 6).

### **Other Real Estate Owned**

Real estate acquired in foreclosure is carried at the lower of cost or the fair market value of the property (less costs to sell), and is included in other assets on the consolidated statements of financial condition. Fair market value is based on independent appraisals and other relevant factors (see Note 20). At the time of acquisition, an excess of cost over fair market value is charged to the allowance for loan losses. Operating expenses are charged to other expense.

Gains and losses of other real estate owned are recognized at the time of the sale or deferred for recognition in future periods, as appropriate, based on the nature of the transaction. Losses on such sales are recognized at the time of the sale.

### **Financial Instruments**

The Bank adopted Accounting Standards Update (ASU) 2016-01, Financial Instruments – Overall (Subtopic 825-10) on January 1, 2019. This standard revises accounting guidance related to the accounting and reporting of financial instruments. Some of the main provisions include: (a) equity

investments that do not result in consolidation and are not accounted for under the equity method would be measured at fair value through net income; (b) changes in instrument-specific credit risk for financial liabilities that are measured under the fair value option would be recognized in other comprehensive income; and (c) elimination of the requirement to disclose the methods and significant assumptions used to estimate the fair value of financial instruments carried at amortized cost; however, it does require the use of exit price when measuring the fair value of financial instruments measured at amortized cost for disclosure purposes. The adoption of this standard did not have a material impact on the Bank's consolidated financial statements.

### **Derivative Financial Instruments**

Derivative instruments are contracts between two or more parties that have a notional and an underlying variable, require no net investment, and allow for the net settlement of positions. Derivative financial instruments are used to meet the ongoing credit needs of customers and the market exposure of certain types of interest rate risk. Derivative instruments are recognized as either assets or liabilities in the consolidated statements of financial condition at fair value. The Bank is a party to various interest rate swaps that are considered derivative instruments. For a fair value hedge, the gain or loss on the derivatives, as well as the offsetting gain or loss on the hedged item, are recognized in current earnings as fair value changes. For stand-alone derivatives that have no hedging designation, changes in the fair value of a derivative are recorded in the consolidated statements of income.

The Bank utilizes forward sales contracts associated with mortgage banking activities in its derivative risk management strategy. The Bank enters into forward sales contracts with brokers/dealers to hedge the risk of changes in fair value, due to changes in interest rates, of both locked residential mortgage loan commitments and residential loans held for sale. The estimated fair value of these derivatives are determined by the changes in the market value of the related loans, caused by changes in market interest rates, during the period from the commitment date or contract date to the valuation date. At December 31, the estimated fair value of rate locks and forward sales agreements were \$46,000 (2019) and \$82,000 (2018) (see Note 18).

The Bank offers interest rate derivative products to certain high-quality commercial borrowers. This product allows customers to enter into an agreement with the Bank to swap their variable rate loan to a fixed rate or vice versa. The Bank limits its risk exposure to these products by entering into a mirror-image, offsetting swap agreement with a separate counterparty. The derivatives are recorded on the statements of the financial position at fair value and changes in fair value of both the customer and the offsetting swap agreements are recorded (and essentially offset) in non-interest income (see Note 18).

### **Income Tax**

The Bank accounts for taxes in accordance with FASB ASC 740-10, resulting in two components of income tax: current and deferred. Current income tax expense approximates taxes to be paid or refunded for the current period. The Bank determines deferred income taxes using the balance sheet method. Under this method, the net deferred tax asset or liability is based on the tax effects of the differences between the book and tax basis of assets and liabilities, and recognizes enacted changes in tax rates and laws in the period in which they occur. Deferred income tax expense results from changes in deferred tax assets and liabilities between periods. At December 31, 2019 and 2018, management has determined that a valuation allowance was unnecessary.

The Bank accounts for uncertainty in income taxes in accordance with FASB ASC 740-10. If the Bank considered that a tax position is "more-likely-than-not" of being sustained upon audit, based solely on the technical merits of the position, it recognizes the tax benefit. The Bank measures the tax benefit by determining the largest amount that is greater than 50% likely of being realized upon settlement, presuming that the tax position is examined by the appropriate taxing authority that has full knowledge of

all relevant information. These assessments can be complex and the Bank obtains assistance from external advisors as necessary. To the extent that the Bank's estimated changes of the final tax outcome of these matters is different than the amounts recorded, such differences will impact the income tax provision in the period in which such determinations are made. If the initial assessment fails to result in the recognition of a tax benefit, the Bank regularly monitors its position and subsequently recognizes the tax benefit if (i) there are changes in tax law or analogous case law that sufficiently raise the likelihood of prevailing on the technical merits of the position to more-likely-than-not, (ii) the statute of limitations expires, or (iii) there is a completion of an audit resulting in a settlement of that tax year with the appropriate agency. Uncertain tax positions are classified as current only when the Bank expects to pay cash within the next twelve months. As of December 31, 2019 and 2018, management of the Bank determined there were no uncertain tax positions.

### **Advertising Costs**

Advertising and promotional costs are expensed when incurred. For the years ended December 31, such costs were \$2,861,000 (2019) and \$2,405,000 (2018).

### **Earnings per Share**

Basic earnings per common share is calculated by dividing net income by the weighted average number of Class A and Class B common shares outstanding during the year (see Note 19).

### **Off-Balance Sheet Credit Related Financial Instruments**

In the ordinary course of business, the Bank has entered into commitments to extend credit, including commercial letters of credit, and standby letters of credit. Such financial instruments are recorded when they are funded.

### **Revenue from Contracts with Customers**

*FASB ASC 606, Revenue from Contracts with Customers* establishes that an entity recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. In general, the new guidance requires companies to use more judgment and make more estimates than under historical guidance, including identifying performance obligations in the contract, estimating the amount of variable consideration to include in the transaction price and allocating the transaction price to each separate performance obligation. The Bank's revenues are primarily composed of interest income on financial instruments, such as loans and investment securities, which are excluded from the scope of FASB ASC 606. The Bank's revenue-generating activities that are within the scope of FASB ASC 606, are presented in Service charges on deposit accounts and in other income on the Bank's consolidated statement of comprehensive Income and are recognized as the Bank satisfies its obligations with the customer. Revenues within the scope of FASB ASC 606 include fiduciary income, interchange income, service charges on deposits, and the sale of other real estate owned. The Bank adopted FASB ASC 606 using the modified retrospective method applied to all contracts not completed as of January 1, 2019. Results for reporting periods beginning after January 1, 2019 are presented under FASB ASC 606 while prior period amounts continue to be reported in accordance with legacy Generally Accepted Accounting Principles (GAAP). The adoption of FASB ASC 606 did not result in a material change to the accounting for any in-scope revenue streams; as such, no cumulative effect adjustment was recorded.

Descriptions of the Bank's revenue-generating activities that are within the scope of FASB ASC 606, which are presented in service charges on deposit accounts and in other income on the Bank's consolidated statement of comprehensive income, are as follows:

- **Service Charges on Deposit Accounts:** The Bank earns fees from its deposit customers from a variety of deposit products and services. Non-transaction based fees such as account maintenance

fees and monthly statement fees are considered to be provided to the customer under a day-to-day contract with ongoing renewals. Revenues for these non-transaction fees are earned over the course of a month, representing the period over which the Bank satisfies the performance obligation. Transaction-based fees such as non-sufficient fund charges, stop payment charges and wire fees are recognized at the time the transaction is executed as the contract duration does not extend beyond the service performed.

- **Wealth Management Services:** The Bank earns fees from customers for fiduciary and investment services provided. Revenues are recognized on a monthly basis and are based on a percentage of the customer's assets under management.
- **Merchant Processing Services and Debit and Credit Card Fees:** The Bank earns fees from cardholder transactions conducted through third party payment network providers which consist of (i) interchange fees earned from the payment network as a debit/credit card issuer, (ii) other fee income, such as late payment fees on credit cards, and (iii) merchant fees earned for customers utilizing the Bank's merchant processing services. These fees are recognized when the transaction occurs, but may settle on a daily or monthly basis.

### Reclassification

Certain reclassifications have been made to the 2018 consolidated financial statements to conform to 2019 classifications. Stockholders' equity, net income, and comprehensive income are unchanged due to these reclassifications.

### NOTE 2 – RESTRICTIONS ON CASH AND DUE FROM BANKS

At December 31, 2019 and 2018, the Bank was not required to maintain average cash balances on hand or with the Federal Reserve Bank.

At December 31, the Bank had \$7,496,000 (2019) and \$573,000 (2018) in cash pledged as collateral to financial institutions for the credit risk of the offset of swap agreements.

### NOTE 3 – INVESTMENT SECURITIES

The carrying amounts of investment securities as shown in the consolidated statements of financial condition of the Bank and their approximate fair values were as follows at December 31:

(in thousands)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
<u>2019</u>				
Available for sale				
U.S. agency securities	\$ 75,300	\$ 622	\$ (194)	\$ 75,728
Mutual funds	29,911	-	(1,326)	28,585
Mortgage-backed securities	23,759	46	(226)	23,579
Other securities	1,396	443	-	1,839
	<u>\$ 130,366</u>	<u>\$ 1,111</u>	<u>\$ (1,746)</u>	<u>\$ 129,731</u>
Held to maturity				
State and municipal securities	\$ 536,805	\$ 25,837	\$ (304)	\$ 562,338
Other securities	4,586	-	(1,586)	3,000
Mortgage-backed securities	392	36	(7)	421
	<u>\$ 541,783</u>	<u>\$ 25,873</u>	<u>\$ (1,897)</u>	<u>\$ 565,759</u>

(in thousands)

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
<u>2018</u>				
Available for sale				
U.S. agency securities	\$ 121,000	\$ 74	\$ (2,310)	\$ 118,764
Mutual funds	29,409	8	(736)	28,681
Mortgage-backed securities	39,110	-	(1,694)	37,416
Other securities	1,452	-	-	1,452
	<u>\$ 190,971</u>	<u>\$ 82</u>	<u>\$ (4,740)</u>	<u>\$ 186,313</u>
Held to maturity				
State and municipal securities	\$ 542,548	\$ 7,314	\$ (7,862)	\$ 542,000
Other securities	4,659	-	(1,403)	3,256
Mortgage-backed securities	454	33	(8)	479
	<u>\$ 547,661</u>	<u>\$ 7,347</u>	<u>\$ (9,273)</u>	<u>\$ 545,735</u>

At December 31, other securities in available for sale include FHLB stock of \$557,000 (2019) and \$553,000 (2018), which is carried at cost. At December 31, this category also included equity securities totaling \$841,000 (2019) and \$900,000 (2018), which are carried at cost because there is no readily available market for these securities.

The scheduled maturities of securities available for sale and securities held to maturity at December 31, 2019 were as follows:

(in thousands)

	Available for Sale		Held to Maturity Securities	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
Due in one year or less	\$ 4,999	\$ 5,006	\$ 29,850	\$ 30,295
Due from one to five years	40,314	40,457	58,378	59,676
Due from five to ten years	18,086	17,759	133,750	139,727
Due after ten years	35,659	36,085	319,805	336,061
	<u>\$ 99,058</u>	<u>\$ 99,307</u>	<u>\$ 541,783</u>	<u>\$ 565,759</u>
Other	31,308	30,424	-	-
<i>Total</i>	<u>\$ 130,366</u>	<u>\$ 129,731</u>	<u>\$ 541,783</u>	<u>\$ 565,759</u>

At December 31, assets, principally securities, carried at cost of \$314,865,000 (2019) and \$357,633,000 (2018), were pledged to secure public deposits, securities sold under repurchase agreements, other borrowings, and for other purposes required or permitted by law.

Reporting comprehensive income requires that an enterprise (a) classify items of other comprehensive income by their nature in a financial statement and (b) display the accumulated balance of other comprehensive income separately from retained earnings and contributed capital in excess of par value in the equity section of a statement of financial condition. The Bank's only item of other comprehensive income is the unrealized gain (loss) on securities available for sale, which is reported net of tax effect on the statement. The net accumulated unrealized holding gain at December 31, 2019 was \$186,000. The net accumulated unrealized holding loss at December 31, 2018 was \$3,509,000. At December 31, 2019, the net change in accumulated unrealized holding losses on available for sale securities was \$4,905,000 with a tax effect of \$1,210,000. At December 31, 2018, the net change in accumulated unrealized holding losses on available for sale securities was \$1,883,000 with a tax effect of \$464,000. During the year ended December 31, 2018, the Bank adopted ASU 2018-02 *Income Statement-Reporting Comprehensive Income (Topic 220): Reclassification of Certain Tax Effects from Accumulated Other Comprehensive*

*Income*, which reclassified \$370,000 from accumulated other comprehensive income to retained earnings due to the tax effects of the Tax Cuts and Jobs Act. During the year ended December 31, 2019, the Bank adopted ASU 2016-01, *Recognition and Measurement of Financial Assets and Financial Liabilities* which reclassified \$1,292,000 of unrealized holding losses on available for sale equity securities from accumulated other comprehensive income to retained earnings.

The following table provides the gross unrealized losses and fair value of temporarily impaired securities, aggregated by investment category and length of time the individual securities have been in a continuous loss position at December 31, 2019.

(in thousands)	Less than 12 months		12 months or more		Total	
	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss
State and municipal securities	\$ 34,098	\$ (301)	\$ 989	\$ (3)	\$ 35,087	\$ (304)
U.S. agency securities	20,813	(135)	11,941	(59)	32,754	(194)
Mortgage-backed securities	3,589	(4)	16,169	(229)	19,758	(233)
Other securities	12	-	2,987	(1,586)	2,999	(1,586)
Mutual funds	-	-	29,911	(1,326)	29,911	(1,326)
<i>Total Temporarily Impaired Securities</i>	<u>\$ 58,512</u>	<u>\$ (440)</u>	<u>\$ 61,997</u>	<u>\$ (3,203)</u>	<u>\$ 120,509</u>	<u>\$ (3,643)</u>

The following table provides the gross unrealized losses and fair value of temporarily impaired securities, aggregated by investment category and length of time the individual securities have been in a continuous loss position at December 31, 2018.

(in thousands)	Less than 12 months		12 months or more		Total	
	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss
State and municipal securities	\$ 117,608	\$ (1,639)	\$ 142,759	\$ (6,223)	\$ 260,367	\$ (7,862)
U.S. agency securities	37,532	(438)	61,275	(1,872)	98,807	(2,310)
Mortgage-backed securities	3,636	(51)	23,169	(693)	26,805	(744)
Other securities	-	-	3,215	(1,403)	3,215	(1,403)
Mutual funds	-	-	37,416	(1,694)	37,416	(1,694)
<i>Total Temporarily Impaired Securities</i>	<u>\$ 158,776</u>	<u>\$ (2,128)</u>	<u>\$ 267,834</u>	<u>\$ (11,885)</u>	<u>\$ 426,610</u>	<u>\$ (14,013)</u>

Unrealized losses at December 31, 2019 and 2018 were due to fluctuations in the market interest rates of U.S. agency and mortgage-backed securities. Management has the intent and ability to hold these investment securities until the fair value or unamortized cost is recovered, which may be maturity, and therefore, does not consider them to be other-than-temporarily impaired at December 31, 2019 and 2018.

Management evaluates securities for other-than-temporary impairment at least on a quarterly basis, and more frequently when economic or market concerns warrant such evaluation. Consideration is given to (1) the length of time and the extent to which the fair value has been less than cost, (2) the financial condition and near-term prospects of the issuer, and (3) the intent and ability of the Bank to retain its investment in the issuer for a period of time sufficient to allow for any anticipated recovery in fair value.

The Bank had two securities that were other-than-temporarily impaired as of December 31, 2019 and 2018. For the year ended December 31, 2019 and 2018, the Bank did not have any gross realized losses from these impaired securities.

## NOTE 4 – LOANS

The Bank's loan portfolio at December 31 consisted of the following:

(in thousands)		2019	2018
Real estate - construction		\$ 375,359	\$ 334,672
Real estate - commercial		952,669	891,310
Real estate - residential		1,118,520	1,017,761
Commercial and industrial		188,076	159,794
Consumer		32,468	26,977
Other		4,894	4,575
	<i>Gross Loans</i>	2,671,986	2,435,089
Less: Allowance for credit losses		(26,072)	(28,506)
Less: Deferred fees		(5,088)	(4,946)
	<i>Net Loans</i>	<u>\$ 2,640,826</u>	<u>\$ 2,401,637</u>

Changes in the allowance for credit losses and recorded investment in financing receivables by loan segment for the year ended December 31, 2019 are summarized as follows:

(in thousands)								
<b>Allowance for credit losses:</b>		Real Estate - Construction	Real Estate - Commercial	Real Estate - Residential	Commercial and Industrial	Consumer	Other	Total
Beginning balance	\$	4,251	\$ 9,161	\$ 10,958	\$ 3,519	\$ 519	\$ 98	\$ 28,506
Charge-offs		(66)	(5)	(494)	(1,420)	(3,638)	(193)	(5,816)
Recoveries		160	338	637	489	1,700	58	3,382
Provision/(reversal)		(216)	(1,130)	(1,958)	907	2,253	144	-
Ending balance	\$	<u>4,129</u>	<u>\$ 8,364</u>	<u>\$ 9,143</u>	<u>\$ 3,495</u>	<u>\$ 834</u>	<u>\$ 107</u>	<u>\$ 26,072</u>
Ending balance: individually evaluated for impairment	\$	<u>708</u>	<u>\$ 114</u>	<u>\$ 149</u>	<u>\$ 91</u>	<u>\$ 96</u>	<u>\$ -</u>	<u>\$ 1,158</u>
Ending balance: collectively evaluated for impairment	\$	<u>3,421</u>	<u>\$ 8,250</u>	<u>\$ 8,994</u>	<u>\$ 3,404</u>	<u>\$ 738</u>	<u>\$ 107</u>	<u>\$ 24,914</u>
<b>Financing receivables:</b>								
Ending loan balance	\$	<u>375,359</u>	<u>\$ 952,669</u>	<u>\$ 1,118,520</u>	<u>\$ 188,076</u>	<u>\$ 32,468</u>	<u>\$ 4,894</u>	<u>\$ 2,671,986</u>
Ending balance: individually evaluated for impairment	\$	<u>11,021</u>	<u>\$ 7,734</u>	<u>\$ 7,747</u>	<u>\$ 972</u>	<u>\$ 175</u>	<u>\$ -</u>	<u>\$ 27,649</u>
Ending balance: collectively evaluated for impairment	\$	<u>364,338</u>	<u>\$ 944,935</u>	<u>\$ 1,110,773</u>	<u>\$ 187,104</u>	<u>\$ 32,293</u>	<u>\$ 4,894</u>	<u>\$ 2,644,337</u>

Changes in the allowance for credit losses and recorded investment in financing receivables by loan segment for the year ended December 31, 2018 are summarized as follows:

(in thousands)

<b>Allowance for credit losses:</b>	Real Estate - Construction	Real Estate - Commercial	Real Estate - Residential	Commercial and Industrial	Consumer	Other	Total
Beginning balance	\$ 3,595	\$ 9,881	\$ 11,564	\$ 2,971	\$ 562	\$ 214	\$ 28,787
Charge-offs	(2)	(5)	(399)	(840)	(3,276)	(17)	(4,539)
Recoveries	378	450	668	557	2,186	19	4,258
Provision/(reversal)	280	(1,165)	(875)	831	1,047	(118)	-
Ending balance	<u>\$ 4,251</u>	<u>\$ 9,161</u>	<u>\$ 10,958</u>	<u>\$ 3,519</u>	<u>\$ 519</u>	<u>\$ 98</u>	<u>\$ 28,506</u>
Ending balance: individually evaluated for impairment	<u>\$ 1,031</u>	<u>\$ 333</u>	<u>\$ 366</u>	<u>\$ 104</u>	<u>\$ 112</u>	<u>\$ -</u>	<u>\$ 1,946</u>
Ending balance: collectively evaluated for impairment	<u>\$ 3,220</u>	<u>\$ 8,828</u>	<u>\$ 10,592</u>	<u>\$ 3,415</u>	<u>\$ 407</u>	<u>\$ 98</u>	<u>\$ 26,560</u>
<b>Financing receivables:</b>							
Ending loan balance	<u>\$ 334,672</u>	<u>\$ 891,310</u>	<u>\$ 1,017,761</u>	<u>\$ 159,794</u>	<u>\$ 26,977</u>	<u>\$ 4,575</u>	<u>\$ 2,435,089</u>
Ending balance: individually evaluated for impairment	<u>\$ 12,831</u>	<u>\$ 8,731</u>	<u>\$ 8,901</u>	<u>\$ 611</u>	<u>\$ 286</u>	<u>\$ -</u>	<u>\$ 31,360</u>
Ending balance: collectively evaluated for impairment	<u>\$ 321,841</u>	<u>\$ 882,579</u>	<u>\$ 1,008,860</u>	<u>\$ 159,183</u>	<u>\$ 26,691</u>	<u>\$ 4,575</u>	<u>\$ 2,403,729</u>

Recorded investment in each risk category of loans by class of loan for the year ended December 31, 2019 is as follows:

(in thousands)	Pass	Special Mention	Substandard	Doubtful	Total
Real estate - construction					
1-4 family residential	\$ 124,730	\$ -	\$ -	\$ -	\$ 124,730
Other construction, land development and land loans	233,225	14,459	2,945	-	250,629
Real estate - commercial					
Nonfarm nonresidential	943,986	4,740	3,943	-	952,669
Real estate - residential					
Revolving lines of credit	367,947	1,587	1,336	-	370,870
1-4 family residential	737,884	6,887	2,879	-	747,650
Commercial and industrial	186,841	348	887	-	188,076
Consumer	32,134	148	186	-	32,468
Other	4,894	-	-	-	4,894
<b>Total</b>	<u>\$ 2,631,641</u>	<u>\$ 28,169</u>	<u>\$ 12,176</u>	<u>\$ -</u>	<u>\$ 2,671,986</u>

Recorded investment in each risk category of loans by class of loan for the year ended December 31, 2018 is as follows:

(in thousands)	Pass	Special Mention	Substandard	Doubtful	Total
Real estate - construction					
1-4 family residential	\$ 111,373	\$ 764	\$ -	\$ -	\$ 112,137
Other construction, land development and land loans	203,187	14,877	4,471	-	222,535
Real estate - commercial					
Nonfarm nonresidential	882,617	3,031	5,662	-	891,310
Real estate - residential					
Revolving lines of credit	376,719	3,085	2,945	-	382,749
1-4 family residential	623,562	9,062	2,388	-	635,012
Commercial and industrial	155,023	3,231	1,540	-	159,794
Consumer	26,472	275	230	-	26,977
Other	4,575	-	-	-	4,575
<i>Total</i>	<u>\$ 2,383,528</u>	<u>\$ 34,325</u>	<u>\$ 17,236</u>	<u>\$ -</u>	<u>\$ 2,435,089</u>

The Bank categorizes each loan into Credit Risk categories based on current financial information, overall debt service coverage, comparison against industry averages, collateral coverage, historical payment experience and current economic trends. The Bank uses the following definitions for Credit Risk ratings:

**Special Mention:** Loans classified as special mention, or watch credits, have a potential weakness or weaknesses that deserve management's close attention. If left uncorrected, these potential weaknesses may result in deterioration of the repayment prospects for the loan or of the institution's credit position at some future date.

**Substandard:** Loans classified as substandard are inadequately protected by the current net worth and paying capacity of the obligor or of the collateral pledged, if any. Loans so classified have a well-defined weakness or weaknesses that jeopardize the liquidation of the debt. They are characterized by the distinct possibility that the institution may sustain some loss if the deficiencies are not corrected.

**Doubtful:** Loans classified as doubtful have all the weaknesses inherent in those classified as substandard, with the added characteristics that the weaknesses make collection or liquidation in full, on the basis of currently existing facts, conditions, and values, highly questionable and improbable.

Credits not covered by the above definition are pass credits, which are not considered to be adversely rated.

An age analysis of past due financing receivables and nonaccrual financing receivables as of December 31, 2019 by loan segment and class are summarized as follows:

(in thousands)	30-59 Days Past Due	60-89 Days Past Due	Greater Than 90 Days Past Due	Total Past Due	Current	Total Financing Receivables	Recorded Investment > 90 Days and Accruing	Nonaccrual Loans
Real estate - construction								
1-4 family residential	\$ -	\$ 698	\$ -	\$ 698	\$ 124,032	\$ 124,730	\$ 49	\$ -
Other construction, land development and land loans	6,489	219	49	6,757	243,872	250,629	-	-
Real estate - commercial	520	488	190	1,198	951,471	952,669	-	252
Real estate - residential Revolving lines of credit	384	-	311	695	370,175	370,870	-	1,942
1-4 family residential	4,213	-	236	4,449	743,201	747,650	-	-
Commercial and industrial	142	37	374	553	187,522	188,075	7	406
Consumer	265	70	-	335	32,133	32,468	-	53
Other	-	-	-	-	4,894	4,894	-	-
<i>Total</i>	<u>\$ 12,013</u>	<u>\$ 1,512</u>	<u>\$ 1,160</u>	<u>\$ 14,685</u>	<u>\$ 2,657,300</u>	<u>\$ 2,671,986</u>	<u>\$ 56</u>	<u>\$ 2,653</u>

An age analysis of past due financing receivables and nonaccrual financing receivables as of December 31, 2018 by loan segment and class are summarized as follows:

(in thousands)	30-59 Days Past Due	60-89 Days Past Due	Greater Than 90 Days Past Due	Total Past Due	Current	Total Financing Receivables	Recorded Investment > 90 Days and Accruing	Nonaccrual Loans
Real estate - construction								
1-4 family residential	\$ -	\$ -	\$ 235	\$ 235	\$ 111,902	\$ 112,137	\$ -	\$ -
Other construction, land development and land loans	1,094	-	-	1,094	221,441	222,535	-	435
Real estate - commercial	75	90	-	165	891,145	891,310	-	2,256
Real estate - residential Revolving lines of credit	2,278	467	925	3,670	379,079	382,749	-	-
1-4 family residential	254	97	434	785	634,227	635,012	-	2,644
Commercial and industrial	1,011	4	-	1,015	158,779	159,794	-	43
Consumer	122	14	-	136	26,841	26,977	-	32
Other	-	-	-	-	4,575	4,575	-	-
<i>Total</i>	<u>\$ 4,834</u>	<u>\$ 672</u>	<u>\$ 1,594</u>	<u>\$ 7,100</u>	<u>\$ 2,427,989</u>	<u>\$ 2,435,089</u>	<u>\$ -</u>	<u>\$ 5,410</u>

Impaired loans as of and for the year ended December 31, 2019 by loan segment are summarized as follows:

(in thousands)	Recorded Investment	Unpaid Principal Balance	Related Allowance	Interest Income Recognized for the Year
With no related allowance recorded:				
Real estate - construction	\$ 9,861	\$ 10,515	\$ -	\$ 478
Real estate - commercial	6,063	6,274	-	395
Real estate - residential	7,568	9,607	-	566
Commercial and industrial	840	1,825	-	97
Consumer	77	444	-	28
With an allowance recorded:				
Real estate - construction	1,160	1,159	708	62
Real estate - commercial	1,671	1,671	113	84
Real estate - residential	179	188	149	10
Commercial and industrial	132	170	93	11
Consumer	98	96	96	7
Total:				
Real estate - construction	<u>\$ 11,021</u>	<u>\$ 11,674</u>	<u>\$ 708</u>	<u>\$ 540</u>
Real estate - commercial	<u>\$ 7,734</u>	<u>\$ 7,945</u>	<u>\$ 113</u>	<u>\$ 479</u>
Real estate - residential	<u>\$ 7,747</u>	<u>\$ 9,795</u>	<u>\$ 149</u>	<u>\$ 576</u>
Commercial and industrial	<u>\$ 972</u>	<u>\$ 1,995</u>	<u>\$ 93</u>	<u>\$ 108</u>
Consumer	<u>\$ 175</u>	<u>\$ 540</u>	<u>\$ 96</u>	<u>\$ 35</u>
<i>Total</i>	<u>\$ 27,649</u>	<u>\$ 31,949</u>	<u>\$ 1,158</u>	<u>\$ 1,738</u>

Impaired loans as of and for the year ended December 31, 2018 by loan segment are summarized as follows:

(in thousands)	Recorded Investment	Unpaid Principal Balance	Related Allowance	Interest Income Recognized for the Year
With no related allowance recorded:				
Real estate - construction	\$ 8,646	\$ 9,381	\$ -	\$ 393
Real estate - commercial	5,384	6,363	-	356
Real estate - residential	8,502	10,923	-	529
Commercial and industrial	462	768	-	50
Consumer	174	875	-	44
With an allowance recorded:				
Real estate - construction	4,185	4,194	1,031	184
Real estate - commercial	3,347	3,433	332	158
Real estate - residential	399	401	366	8
Commercial and industrial	149	180	106	11
Consumer	112	112	112	8
Total:				
Real estate - construction	<u>\$ 12,831</u>	<u>\$ 13,575</u>	<u>\$ 1,031</u>	<u>\$ 577</u>
Real estate - commercial	<u>\$ 8,731</u>	<u>\$ 9,796</u>	<u>\$ 332</u>	<u>\$ 514</u>
Real estate - residential	<u>\$ 8,901</u>	<u>\$ 11,324</u>	<u>\$ 366</u>	<u>\$ 537</u>
Commercial and industrial	<u>\$ 611</u>	<u>\$ 948</u>	<u>\$ 106</u>	<u>\$ 61</u>
Consumer	<u>\$ 286</u>	<u>\$ 987</u>	<u>\$ 112</u>	<u>\$ 52</u>
<i>Total</i>	<u>\$ 31,360</u>	<u>\$ 36,630</u>	<u>\$ 1,947</u>	<u>\$ 1,741</u>

The majority of impaired loans requiring an allowance are measured using the fair value of the underlying collateral since these loans are considered collateral dependent. Any unsecured loans are measured using discounted cash flow analysis of the payments expected over the life of the loan, considering any internal

or external factors that currently exist that would impact the amount or timing of cash flows. The average monthly recorded investment in impaired loans for the years ended December 31 was \$27,815,000 (2019) and \$33,505,000 (2018). When the ultimate collectability of the total principal of an impaired loan is in doubt and the loan is on nonaccrual status, all payments are applied to principal under the cost recovery method.

Troubled debt restructurings by loan segment as of December 31, 2019 consisted of the following:

(in thousands)	Number of Contracts at Year End	Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment
Real estate - construction	11	\$ 11,222	\$ 10,931
Real estate - commercial	8	6,442	6,310
Real estate - residential	22	5,639	4,706
Commercial and industrial	5	734	588
Consumer	3	371	85
<i>Total</i>	<u>49</u>	<u>\$ 24,408</u>	<u>\$ 22,620</u>

There were no troubled debt restructurings which subsequently re-defaulted during the year ended December 31, 2019.

Troubled debt restructurings by loan segment as of December 31, 2018 consisted of the following:

(in thousands)	Number of Contracts at Year End	Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment
Real estate - construction	12	\$ 13,166	\$ 12,272
Real estate - commercial	7	7,082	6,749
Real estate - residential	21	3,078	2,985
Commercial and industrial	7	681	584
Consumer	8	185	92
<i>Total</i>	<u>55</u>	<u>\$ 24,192</u>	<u>\$ 22,682</u>

Troubled debt restructurings which subsequently re-defaulted during the year ended December 31, 2018 consisted of the following:

(in thousands)	Number of Contracts at Year End	Recorded Investment
Real estate - construction	-	\$ -
Real estate - commercial	-	-
Real estate - residential	1	699
Consumer	-	-
<i>Total</i>	<u>1</u>	<u>\$ 699</u>

At December 31, 2019, there are no commitments to lend additional funds to any borrower whose loan term has been modified in a troubled debt restructuring.

From time to time, the Bank pledges real estate loans to government agencies to collateralize other borrowings. At December 31, loans of \$442,613,000 (2019) and \$395,643,000 (2018) were pledged.

At December 31, customer overdraft accounts included in installment loans were \$21,669,000 (2019) and \$1,951,000 (2018). The increase in Overdrafts is the result of a customer's error when attempting to draw on their secured line of credit. The Overdraft was cleared on the first business day of 2020.

**NOTE 5 – BANK PROPERTY, EQUIPMENT, AND LEASEHOLD IMPROVEMENTS**

The Bank's property, equipment, and leasehold improvements at December 31, consisted of the following:

(in thousands)	2019	2018
Land, building, and leasehold improvements	\$ 80,214	\$ 78,260
Furniture and equipment	51,277	45,091
Safe deposit and vault equipment	1,992	1,971
Property and equipment of limited liability companies	20,267	19,780
	153,750	145,102
Less: accumulated depreciation	(82,780)	(75,103)
	70,970	69,999
Construction in progress	1,565	4,550
<i>Total</i>	\$ 72,535	\$ 74,549

At December 31, the Bank had construction in process of \$1,565,000 (2019) and \$4,550,000 (2018). Estimated cost to complete these projects at December 31 is \$4,489,000 (2019), \$3,211,000 (2018), and is related to architectural design for new branches, remodeling of bank locations, and technology projects.

For the years ended December 31, consolidated depreciation expense was \$8,595,000 (2019) and \$7,078,000 (2018).

The Bank leases certain buildings and land for its bank locations under long-term leases. These leases are operating leases with terms ranging from one to ten years and provide rate increases based on the consumer price index and, in one lease, changes in the prime rate of interest.

As of December 31, 2019 the Bank's lease ROU assets and related lease liabilities were \$13 million and \$13.3 million, respectively.

The table below summarized information related to the Bank's operating leases at December 31:

	2019
Weighted average remaining lease term of operating leases, in years	8.21
Weighted average discount rate of operating leases	3.00%

The following is a schedule by year of future minimum rental payments, not including extensions, required under the operating leases:

(in thousands)	
2020	\$ 4,206
2021	2,046
2022	1,976
2023	1,627
2024 and thereafter	5,941
<i>Total</i>	\$ 15,796

For the years ended December 31, rent expense from operating leases was \$4,088,000 (2019) and \$3,628,000 (2018).

Included above are certain leases between the Bank and separate entities for buildings occupied by certain bank locations. The Bank and these entities are related by common ownership (see Note 14). The combined rent for these leases for December 31 was \$1,513,000 (2019) and \$1,355,000 (2018) and are eliminated in consolidation.

**NOTE 6 – GOODWILL**

Goodwill of \$17,631,000 was acquired in 2006 and is subject to annual impairment testing. The Bank has selected September 30 as the annual impairment testing date. Based on the results of the annual impairment testing, goodwill was not considered to be impaired as of December 31, 2019 and 2018.

**NOTE 7 – CERTIFICATES OF DEPOSIT**

At December 31, the aggregate amount of time deposits in denominations that meet or exceed the FDIC insurance limit of \$250,000 were \$35,762,000 (2019) and \$38,980,000 (2018).

Scheduled maturities of all certificates of deposit at December 31 are as follows:

(in thousands)		
2020	\$	89,684
2021		34,765
2022		7,284
2023		4,257
2024 and thereafter		<u>2,527</u>
	<i>Total</i> \$	<u><u>138,517</u></u>

**NOTE 8 – REPURCHASE AGREEMENTS**

During the years ending December 31, 2019 and 2018, the Bank entered into collateralized overnight repurchase accounts with select customers under repurchase contracts. At December 31, account balances totaled \$37,071,000 (2019) and \$39,067,000 (2018). All of the repurchase accounts are settled nightly and all of the accounts are collateralized with U.S. agency bonds. As of December 31, the pledged bonds that are actively being used to secure the deposits had a market value of \$58,326,000 (2019) and \$74,563,000 (2018). The Bank monitors the account balances and the pledged collateral market values on a daily basis to ensure adequate collateral is pledged. Collateral value fluctuations are mitigated by pledging only U.S. agency bonds and by pledging a ladder of bond maturities.

**NOTE 9 – FHLB LINE OF CREDIT AND DRAWDOWN AGREEMENT**

The Bank has an available line of credit with the FHLB. Interest is charged at the FHLB’s floating interest rate. As of December 31, 2019 and 2018, the Bank had no outstanding draws. As of December 31, 2019, the Bank had borrowing capacity on the line of \$335,772,000.

The Bank has an agreement with a financial institution in which the Bank can request funds and the funds will be sent through wire transfer. The drawdown wire per-transaction dollar limit is \$25,000,000. There is no set maturity date for the agreement. The Bank has cash pledged to the agreement of \$250,000. As of December 31, 2019 and 2018, the Bank had no outstanding draws.

## NOTE 10 – SUBORDINATED DEBENTURES

The Bank’s subordinated debentures at December 31 consisted of the following:

(in thousands)	2019	2018
Subordinated debenture due January 2029, with interest at 9.5%; principal due at maturity, interest payments due quarterly.	\$ 10,413	\$ 10,413
Subordinated debenture due November 2034, with interest at three-month LIBOR plus 2.85% and repriced quarterly (4.84% and 5.29% at December 31, 2019 and 2018, respectively); principal due at maturity, interest payments due quarterly.	10,310	10,310
Subordinated debenture due March 2036, with interest at three-month LIBOR plus 1.30% (3.19% and 4.09% at December 31, 2019 and 2018, respectively); principal due at maturity, interest payments due quarterly.	25,774	25,774
Subordinated debenture due December 2036, with interest at three-month LIBOR plus 1.71% and repriced quarterly (3.60% and 4.50% at December 31, 2019 and 2018, respectively); principal due at maturity, interest payments due quarterly.	12,372	12,372
Subordinated debenture due June 2038, with interest at three-month LIBOR plus 3.50% and repriced quarterly (5.39% and 6.29% at December 31, 2019 and 2018, respectively); principal due at maturity, interest payments due quarterly.	10,310	10,310
<i>Total</i>	<u>\$ 69,179</u>	<u>\$ 69,179</u>

At December 31, 2019 and 2018, the Bank had an equity investment in business trusts of \$2,091,000. Under FASB ASC 810-10, the business trusts, which had been formed for the sole purpose of issuing trust preferred securities, are not consolidated.

## NOTE 11 – COMMON STOCK

In August 1998, the Bank amended its Articles of Incorporation for the creation of a second, non-voting class of stock, known as Class B common stock (all voting common stock being re-designated as Class A common stock). The Bank can authorize a right of refusal on certain transfers of Class A and Class B common stock.

In April 2019, the Bank listed the Class B non-voting common stock for trading on the OTC Pink Market, with a trading symbol of ALPIB. The Class A voting common stock is not traded on any securities market.

## NOTE 12 – EMPLOYEE STOCK OWNERSHIP AND 401(K) PLAN

The Bank established an employee stock ownership plan (the Plan) effective January 1, 1983, and was amended January 1, 2008, for the benefit of its eligible employees and their beneficiaries under section 401(a) of the Internal Revenue Code (“IRC”). The Plan is subject to the provisions of the Employee Retirement Income Security Act of 1974 (“ERISA”). The Plan is designed with two components: an ESOP and 401(k). The ESOP is designed to invest primarily in qualifying employer securities (“Bank Stock”), as defined in IRC Section 409(1). The 401(k) provides eligible employees a qualified cash or deferred arrangement as defined in IRC section 401(k).

Employees of the Bank become eligible to participate in the 401(k) component of the Plan upon completion of three months of service. Employees become eligible for the ESOP component of the Plan upon completion of one year of service. One year of service is defined as a twelve consecutive month period during which the employee completes not less than 1,000 hours of service.

The ESOP component of the Plan is a non-contributory plan that is funded by the Bank with Bank stock or cash. The amount of the contribution is determined annually by the Bank's Board of Directors. For the years ended December 31, the Bank contributed \$3,541,000 (2019) and \$3,252,000 (2018), to the Plan. The amount contributed to the plan is recorded as compensation expense by the Bank. Forfeitures, if any, are reallocated among remaining participants. Dividends on ESOP shares are recorded as a reduction of retained earnings.

As of December 31, shares in the ESOP were 21,818 (2019) and 22,204 (2018). ESOP shares are included in the earnings per share computation.

The Bank stock that is held by the Plan and its participants includes a put option. The put option is a right to demand that the Bank buy any shares of its stock distributed to participants. The put price is representative of the fair value of the stock. The Bank can pay for the purchase, with interest, over a period of five years. These distributions are available upon retirement, death, disability, or termination of employment.

For the ESOP component, a participant's accrued benefit derived from the Bank's contributions shall be 100% vested after attaining normal retirement age, or if the employee terminates as a result of death or disability. If a participant's employment terminates prior to normal retirement age or for any reason other than death or disability, then, for each year of service they shall be vested in their account based on continuous years of service at 20% per year, beginning at the end of year two and becoming fully vested at the end of year six.

For the 401(k) component of the Plan, participants may elect to defer before-tax contributions up to 75% of their annual compensation, not to exceed annual limits as determined by the Internal Revenue Service ("IRS"). Participants age 50 or older may also elect to defer additional catch-up contributions to the Plan, which are limited by the IRS. Participants are 100% vested in their voluntary contributions and actual earnings or losses thereon.

Distributions are available upon retirement, death, disability, attainment of age 59 ½, or termination of employment. Distributions from the ESOP component of the Plan will be made either in Bank stock or cash. The Plan's ESOP distribution policy dictates the period over which participants are paid based on their event of termination and the vested account balance at termination. The participant will receive the 401(k) component, equal to the participant's vested account balance, in either a lump sum or in installment distributions based on the participant's election. If the participant's total vested balance, including the ESOP and the 401(k) components combined, is greater than \$1,000, the participant may elect not to receive a distribution until required by law to receive required minimum distributions.

## NOTE 13 – INCOME TAXES

The bank files a consolidated federal income tax return. The consolidated provision for income taxes consisted of the following for the years ended December 31:

(in thousands)	2019	2018
Current tax provision		
Federal	\$ 8,458	\$ 8,596
State	2,253	2,341
	10,711	10,917
Deferred	1,621	1,202
<i>Income Tax Provision</i>	\$ 12,332	\$ 12,119

At December 31, the income tax provision for the consolidated financial statements results in an effective rate, which varies from the normal statutory corporate rate of 21% for federal income taxes and state income tax of 4.6%. The reason for these differences are as follows:

(in thousands)	2019	2018
Statutory rate	\$ 17,346	\$ 16,515
Permanent differences – primarily tax-exempt interest income, earnings on life insurance and amortization on core deposit intangibles	(3,470)	(4,584)
Other	(1,544)	188
<i>Income Tax Provision</i>	\$ 12,332	\$ 12,119

The components of the deferred tax asset and the deferred tax liability are as follows at December 31:

(in thousands)	2019	2018
Deferred tax asset:		
Federal	\$ 11,303	\$ 14,390
State	3,010	1,968
	14,313	16,358
Deferred tax liability:		
Federal	(4,343)	(4,138)
State	(1,156)	(574)
	(5,499)	(4,712)
Deferred tax asset, net	\$ 8,814	\$ 11,646

Deferred income taxes reflect the net tax effects of temporary differences between carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax reporting. Significant components of the Bank's deferred tax assets and liabilities are as follows:

(in thousands)	2019	2018
Deferred tax assets:		
Allowance for loan losses	\$ 6,429	\$ 7,031
Deferred compensation	3,785	4,510
Net unrealized loss on available for sale securities	381	1,149
Net unrealized loss on other real estate owned	626	478
Other	3,092	3,190
<i>Total Deferred Tax Assets</i>	14,313	16,358
Deferred tax liabilities:		
Accelerated depreciation	(4,023)	(3,365)
Prepaid expenses	(533)	(487)
Other	(943)	(860)
<i>Total Deferred Tax Liabilities</i>	(5,499)	(4,712)
<i>Deferred Tax Asset, Net</i>	\$ 8,814	\$ 11,646

At December 31, 2019, the Bank had no tax carryforwards.

## NOTE 14 – RELATED PARTY TRANSACTIONS

In the ordinary course of business, the Bank has loans receivable from directors and executive officers of the Bank and their affiliates. Interest rates on loans are based upon the Bank's base rate and are negotiated on an individual basis. Loans to related parties were as follows:

(in thousands)	2019	2018
Balance at January 1	\$ 8,676	\$ 9,336
New loans, including renewals	919	562
Payments, including renewals	(1,048)	(1,222)
Balance at December 31	<u>\$ 8,547</u>	<u>\$ 8,676</u>

Terms and rates of interest on deposit accounts are similar to those extended to unrelated Bank customers. At December 31, related party deposits were \$9,978,000 (2019) and \$9,306,000 (2018).

The Bank leases buildings from separate entities related by common ownership (see Note 5).

## NOTE 15 – DEFERRED COMPENSATION AND SALARY CONTINUATION PLAN

Effective January 1, 1990, the Bank adopted a deferred compensation plan (the Compensation Plan) for certain key executives. The Compensation Plan is a nonqualified executive benefit plan in which the eligible bank officer or director voluntarily elects to defer some or all of his or her current compensation in exchange for the Bank's promise to pay a deferred benefit sometime in the future. Under this type of plan, the deferred fees or salaries are expensed by the Bank and set aside in a separate liability account and interest is periodically credited on the account balance. Benefits are payable under certain conditions and in amounts set forth by the Compensation Plan. As of December 31, the Bank reflected a liability, which is included in the accompanying consolidated statements of financial condition as part of other liabilities, of \$15,348,000 (2019) and \$18,290,000 (2018) in connection with the Compensation Plan. The Compensation Plan is an unfunded plan, which means that the employee has no rights under the agreement beyond those of a general creditor of the Bank, and there are no specific assets set aside by the Bank in connection with the Compensation Plan.

The Compensation Plan is informally linked with a single premium universal life insurance policy on the life of each participant, which has been purchased by the Bank in connection with the implementation of the Compensation Plan.

The Bank also adopted a salary continuation plan (the Continuation Plan) for certain key executives. The Continuation Plan provides, among other things, that if the executive remains with the Bank until retirement, the Bank will pay the scheduled benefits. The Continuation Plan terminates if the employee leaves the Bank prior to retirement. This Continuation Plan is also linked informally with life insurance policies acquired by the Bank. As of December 31, the Bank reflected a liability, which is included in the accompanying consolidated statements of financial condition as part of other liabilities, of \$2,948,000 (2019) and \$2,855,000 (2018) in connection with the Continuation Plan. The Continuation Plan is an unfunded plan, which means that the employee has no rights under the agreement beyond those of a general creditor of the Bank, and there are no specific assets set aside by the Bank in connection with the Continuation Plan. For the years ended December 31, the Continuation Plan expense was \$275,000 (2019) and \$138,000 (2018).

## **NOTE 16 – COMMITMENTS AND CONTINGENT LIABILITIES**

In the normal course of business, the Bank is involved in various legal actions arising from its lending and collection activities. In the opinion of management, the outcome of these legal actions will not significantly affect the consolidated financial condition of the Bank.

The Bank's consolidated financial statements do not reflect various commitments and contingent liabilities which arise in the normal course of business and which involve elements of credit risk, interest rate risk and liquidity risk.

In the normal course of business, the Bank is a party to certain off-balance sheet financial instruments to meet the needs of its customers. These financial instruments involve, to varying degrees, elements of credit and market risk in excess of the amount recorded on the consolidated statements of financial condition. The Bank does not anticipate that losses, if any, as a result of credit risk or market risk, would materially affect the consolidated stockholders' equity position of the Bank.

Credit risk represents the maximum potential loss the Bank faces due to possible non-performance by obligors and counterparties of the terms of their contracts. Market risk represents the potential loss the Bank faces due to the decrease in the value of an off-balance sheet financial instrument caused primarily by changes in interest rates.

Credit risk is represented by the contractual amount of the letters of credit and commitments to extend credit. Letters of credit and commitments to extend credit have market risk if issued or extended at a fixed rate of interest. However, these contracts are primarily made at a variable rate of interest.

The majority of the Bank's loan portfolio and collateral for those loans is concentrated in Colorado. However, obligors and counterparties are diversified nationally. Because of this, the risks of lending reflect both general and local economic conditions.

Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Since many of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. The amount of collateral obtained, if it is deemed necessary by the Bank upon extension of credit, is based on management's credit evaluation of the counterpart. Collateral held varies, however may include accounts receivable, inventory, property, plant, and equipment, and income-producing residential and commercial properties.

Standby letters of credit and financial guarantees written are conditional commitments issued by the Bank to guarantee the performance of a customer to a third party. At December 31, standby letters of credit, loan commitments, and unused lines of credit were \$788,783,000 (2019) and \$728,444,000 (2018).

## **NOTE 17 – CAPITAL REQUIREMENTS**

The Bank is subject to various regulatory capital requirements administered by the federal banking agencies. Failure to meet minimum capital requirements can initiate certain mandatory, and possibly additional discretionary, actions by regulators that, if undertaken, could have a direct material effect on the Bank's consolidated financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Bank must meet specific capital guidelines that involve quantitative measures of the Bank's assets, liabilities, and certain off-balance-sheet items as calculated

under regulatory accounting practices. The Bank's capital amounts and classification are also subject to qualitative judgments by the regulators about components, risk weightings, and other factors.

Quantitative measures, established by regulation to ensure capital adequacy, require the Bank to maintain minimum amounts and ratios (set forth in the table below). Management believes, as of December 31, 2019, the Bank meets all capital adequacy requirements to which it is subject.

In 2013, the Federal Reserve voted to adopt final capital rules implementing Basel III requirements for U.S. Banking organizations. Under the final rule, minimum requirements increased for both the quantity and quality of capital held by banking organizations. Consistent with the international Basel framework, the final rule included a new minimum ratio of common equity tier 1 capital to risk-weighted assets, the most loss-absorbing form of capital, and implements strict eligibility criteria for regulatory capital instruments. The final rule modified the methodology for calculating risk-weighted assets to enhance risk sensitivity. The Bank used risk weighting to assign different levels of risk to different classes of assets. The rule has raised the minimum ratio of tier 1 capital to risk-weighted assets and includes a minimum leverage ratio of 4%. These new minimum capital ratios were effective on January 1, 2015 and were fully phased by January 1, 2019.

As of September 30, 2019, in accordance with Basel III, the Bank was categorized as well capitalized under the regulatory framework for prompt corrective action. To be categorized as well capitalized, the Bank must maintain minimum common equity tier 1 risk-based capital, total risk-based capital, Tier I risk-based capital, and Tier I capital leverage ratios as set forth in the following table. There are no conditions or events since that notification that management believes have changed the Bank's category.

(in thousands)	Actual		For Capital Adequacy Purposes		To Be Well Capitalized Under Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
As of December 31, 2019:						
Common Equity Tier 1 Risk-Based Capital (to Risk Weighted Assets)						
Alpine Bank	\$ 377,099	12.72%	\$ 133,381	4.50%	\$ 192,661	6.50%
Alpine Banks of Colorado	\$ 324,625	10.94%	\$ 133,517	4.50%	\$ 192,858	6.50%
Total Risk Based Capital (to Risk Weighted Assets)						
Alpine Bank	\$ 403,619	13.62%	\$ 237,121	8.00%	\$ 296,402	10.00%
Alpine Banks of Colorado	\$ 418,246	14.10%	\$ 237,364	8.00%	\$ 296,705	10.00%
Tier 1 Risk-Based Capital (to Risk Weighted Assets)						
Alpine Bank	\$ 377,098	12.72%	\$ 177,841	6.00%	\$ 237,111	8.00%
Alpine Banks of Colorado	\$ 391,725	13.20%	\$ 178,023	6.00%	\$ 237,364	8.00%
Tier 1 Risk-Based Capital (to Average Assets) – Leverage Ratio						
Alpine Bank	\$ 377,098	9.93%	\$ 151,939	4.00%	\$ 189,924	5.00%
Alpine Banks of Colorado	\$ 391,725	10.31%	\$ 151,973	4.00%	\$ 189,967	5.00%

(in thousands)	Actual		For Capital Adequacy Purposes		To Be Well Capitalized Under Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
As of December 31, 2018:						
Common Equity Tier 1 Risk-Based Capital (to Risk Weighted Assets)						
Alpine Bank	\$ 333,376	12.24%	\$ 122,542	4.50%	\$ 177,005	6.50%
Alpine Banks of Colorado	\$ 280,081	10.27%	\$ 122,702	4.50%	\$ 177,234	6.50%
Total Risk Based Capital (to Risk Weighted Assets)						
Alpine Bank	\$ 362,248	13.30%	\$ 217,853	8.00%	\$ 272,316	10.00%
Alpine Banks of Colorado	\$ 367,054	13.37%	\$ 218,137	8.00%	\$ 272,671	10.00%
Tier 1 Risk-Based Capital (to Risk Weighted Assets)						
Alpine Bank	\$ 333,376	12.24%	\$ 163,390	6.00%	\$ 217,853	8.00%
Alpine Banks of Colorado	\$ 347,181	12.73%	\$ 163,602	6.00%	\$ 218,137	8.00%
Tier 1 Risk-Based Capital (to Average Assets) – Leverage Ratio						
Alpine Bank	\$ 333,376	9.23%	\$ 144,434	4.00%	\$ 180,543	5.00%
Alpine Banks of Colorado	\$ 347,181	9.61%	\$ 144,479	4.00%	\$ 180,599	5.00%

## NOTE 18 – DERIVATIVE FINANCIAL INFORMATION

The Bank offers interest rate derivative products (e.g. interest rate swaps) to certain of its high-quality commercial borrowers. This product allows customers to enter into an agreement with the Bank to swap their variable rate loan to a fixed rate or vice versa. These derivative products are designed to reduce, eliminate or modify the risk of changes in the borrower's interest rate or market price risk. The extension of credit incurred through the execution of these derivative products is subject to the same approvals and underwriting standards as the related traditional credit product. The Bank limits its risk exposure to these products by entering into a mirror-image, offsetting swap agreement with a separate, well capitalized and rated counterparty previously approved by the Chief Financial Officer. By using these interest rate swap arrangements, the Bank is also better insulated from the interest rate risk associated with underwriting fixed-rate loans.

Commitments to fund certain mortgage loans (interest rate locks) to be sold into the secondary market and forward commitments for the future delivery of mortgage loans to third party investors are considered derivatives. It is the Bank's practice to enter into forward commitments for the future delivery of residential mortgage loans when interest rate lock commitments are entered into in order to economically hedge the effect of changes in interest rates resulting from its commitments to fund the loans. The estimated fair value of these derivatives are determined by the changes in the market value of the related loans, caused by changes in market interest rates, during the period from the commitment date or contract date to the valuation date.

These derivative contracts are not designated against specific assets or liabilities under FASB ASC 815-10 and, therefore, do not qualify for hedge accounting. The derivatives are recorded on the consolidated statements of financial condition at fair value and changes in fair value essentially offset in non-interest income.

The following table presents the notional amount and fair value of the Bank's derivative instruments held or issued in connection with customer-initiated and mortgage banking activities:

(in thousands)	December 31, 2019		December 31, 2018	
	Notional Amount	Fair Value	Notional Amount	Fair Value
Included in other assets:				
Customer-initiated and mortgage banking derivatives:				
Customer-initiated derivatives	\$ 163,045	\$ 7,907	\$ 144,017	\$ 3,468
Forward contracts related to mortgage loans to be delivered for sale	-	-	3,961	41
Interest rate lock commitments	25,200	46	6,767	41
<i>Total derivatives included in other assets</i>	<u>\$ 188,265</u>	<u>\$ 7,953</u>	<u>\$ 154,745</u>	<u>\$ 3,550</u>
Included in other liabilities:				
Customer-initiated and mortgage banking derivatives:				
Customer-initiated derivatives	\$ 163,045	\$ 7,907	\$ 144,017	\$ 3,468
Forward contracts related to mortgage loans to be delivered for sale	8,768	9	1,488	4
Interest rate lock commitments	2,477	1	3,166	12
<i>Total derivatives included in other liabilities</i>	<u>\$ 174,292</u>	<u>\$ 7,917</u>	<u>\$ 148,671</u>	<u>\$ 3,484</u>

## NOTE 19 – STOCKHOLDERS' EQUITY

### Earnings Per Common Share

The following table illustrates the reconciliation of weighted average shares used for earnings per common share computations for the years ended December 31, 2019, 2018 and 2017:

	2019	2018	2017
Numerator:			
Net income	<u>\$ 58,008</u>	<u>\$ 54,851</u>	<u>\$ 33,364</u>
Denominator:			
Weighted-average number of commons shares outstanding – basic	<u>\$ 104,866</u>	<u>\$ 105,480</u>	<u>\$ 105,869</u>
Earnings per common share:			
Basic	\$ 553	\$ 520	\$ 318

### Dividends

The timing and amount of cash dividends paid on the Bank's common stock depends on the Bank's earnings, capital requirements, financial condition and other relevant factors. Dividends on common stock from the Bank depends substantially upon receipt of dividends from Alpine, the wholly-owned bank subsidiary, which is the Bank's predominant source of income.

The following table summarizes the dividend activity for the years ended December 31, 2019, 2018 and 2017:

Declared	Cash Dividend per Share	Record Date	Paid Date
January 19, 2017	\$25.00	December 31, 2016	January 19, 2017
April 13, 2017	\$25.00	March 31, 2017	April 13, 2017
July 13, 2017	\$25.00	June 30, 2017	July 13, 2017
October 12, 2017	\$25.00	September 30, 2017	October 12, 2017
January 11, 2018	\$27.00	December 31, 2017	January 11, 2018
April 12, 2018	\$27.00	March 31, 2018	April 12, 2018
July 12, 2018	\$27.00	June 30, 2018	July 12, 2018
October 11, 2018	\$27.00	September 30, 2018	October 11, 2018
January 17, 2019	\$29.00	December 31, 2018	January 17, 2019
April 11, 2019	\$29.00	April 22, 2019	April 23, 2019
July 11, 2019	\$29.00	July 22, 2019	July 26, 2019
October 10, 2019	\$29.00	October 21, 2019	October 25, 2019

The FDIC and the Colorado Division of Banking have the authority under their supervisory powers to prohibit the payment of dividends by Alpine to the Bank. Additionally, current guidance from the Board of governors of the Federal Reserve System provides, among other things, that dividends per share on the Bank's common stock generally should not exceed earnings per share, measured over the previous four fiscal quarters. Current regulations allow the Bank and Alpine to pay dividends on their common stock if the Bank's or Alpine's regulatory capital would not be reduced below the statutory capital requirements set by the Federal Reserve and the FDIC.

#### **NOTE 20 – FAIR VALUES OF FINANCIAL INSTRUMENTS**

In accordance with the Fair Value Measurements of FASB ASC 820-10, assets and liabilities are grouped in three levels, based on the markets in which the assets and liabilities are traded and the reliability of the assumptions used to determine fair value. These levels are:

- Level 1 – Valuation is based upon quoted prices for identical instruments traded in active markets.
- Level 2 – Valuation is based upon quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active, and model-based valuation techniques for which all significant assumptions are observable in the market.
- Level 3 – Valuation is generated from model-based techniques that use significant assumptions not observable in the market. These unobserved assumptions reflect the Bank's own estimates of assumptions that market participants would use in pricing the asset or liability. Valuation techniques include use of option pricing models, discounted cash flow models and similar techniques.

In accordance with the Fair Value Measurements and Disclosures topic of the Codification, the Bank bases fair values on the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Fair value measurements for assets and liabilities where there exists limited or no observable market data and, therefore, are based primarily upon the Bank's estimates, are often calculated based on current pricing policy, the economic and competitive environment, the characteristics of the asset or liability and other such factors. Therefore, the results cannot be determined with precision and may not be realized in an actual sale or immediate settlement of the asset or liability. Additionally, there may be inherent weaknesses in any calculation technique, and changes in the underlying assumptions used, including discount rates and estimates of future cash flows, that could significantly affect the results of current or future values.

The following is a description of valuation methodologies used for assets and liabilities recorded at fair value and for estimating fair value for financial instruments not recorded at fair value:

Cash and due from banks and federal funds sold. These assets are carried at historical cost. The carrying amount is a reasonable estimate of fair value because of the relatively short time between the origination of the instrument and its expected realization.

Securities to be held to maturity and available for sale. Securities held to maturity are recorded at amortized cost while securities available for sale are recorded at fair value on a recurring basis. Fair value measurement is based upon quoted prices, if available. If quoted prices are not available, fair values are measured using independent pricing models or other model-based valuation techniques such as the present value of future cash flows, adjusted for the security's credit rating, prepayment assumptions and other factors such as credit loss assumptions. Level 1 securities include those traded on an active exchange for identical securities that the Bank has the ability to access at the measurement date and consist of mutual funds. Level 2 securities consist of U.S. government and agency debt securities, agency mortgage-backed securities, corporate debt securities and other securities.

Loans receivable. The Bank does not record loans at fair value. However, from time to time, the Bank will record nonrecurring fair value adjustments to loans to reflect (1) partial write-downs that are based on observable market price or current appraised value of the collateral, or (2) the full charge-off of the loan carrying value.

Fair values for impaired loans are estimated using discounted cash flow analyses or underlying collateral values, where applicable. As such, the Bank classifies impaired loans subject to nonrecurring fair value adjustments as Level 3.

Loans held for sale. Loans held for sale are carried at fair value. The fair value of loans held for sale is based on what secondary markets are currently offering for portfolios with similar characteristics.

Other Real Estate Owned (OREO). OREO represents real property taken by the Bank either through foreclosure or through a deed in lieu from the borrower. The fair value of OREO is primarily based on property appraisals less costs to sell. The appraised value may further be adjusted by management based on relevant facts and circumstances to reflect current market conditions. Because of the high degree of judgement required in estimating the fair value of OREO it is considered a Level 3 classification.

Derivative financial instruments. Customer-initiated derivatives valuations are derived from third-party models whose significant inputs are readily observable market parameters, primarily yield curves. These fair value measurements are classified as Level 2.

Deposit liabilities. Deposit liabilities are carried at historical cost. FASB ASC 825-10 states that the fair value of deposits with no stated maturity, such as noninterest-bearing demand deposits, interest-bearing checking, and market rate and other savings, is equal to the amount payable on demand at the measurement date.

Mortgage banking related derivatives, including commitments to fund mortgage loans (interest rate locks) to be sold into the secondary market and forward commitments for the future delivery of these mortgage loans, are recorded at fair value on a recurring basis. The fair value of these commitments is based on the fair value of related mortgage loans determined using observable market data. Interest rate lock commitments are adjusted for expectations of exercise and funding (this adjustment is not considered to be a material input). Valuations on mortgage banking derivatives are classified as Level 2.

Fair value measurements for assets recorded at fair value on a recurring basis at December 31, are as follows:

(in thousands)	Fair Value	Level 1	Level 2	Level 3
<u>2019</u>				
Securities available-for-sale	\$ 129,731	\$ 28,585	\$ 101,146	\$ -
Loans held for sale	14,999	-	14,999	-
Derivative assets:				
Customer-initiated derivatives	7,907	-	7,907	-
Forward contracts related to mortgage loans to be delivered for sale	-	-	-	-
Interest rate lock commitments	46	-	46	-
Total assets at fair value	<u>\$ 152,683</u>	<u>\$ 28,585</u>	<u>\$ 124,098</u>	<u>\$ -</u>
Derivative liabilities:				
Customer-initiated derivatives	7,907	-	7,907	-
Forward contracts related to mortgage loans to be delivered	9	-	9	-
Interest rate lock commitments	1	-	1	-
<i>Total liabilities at fair value</i>	<u>\$ 7,917</u>	<u>\$ -</u>	<u>\$ 7,917</u>	<u>\$ -</u>
(in thousands)	Fair Value	Level 1	Level 2	Level 3
<u>2018</u>				
Securities available-for-sale	\$ 186,313	\$ 37,416	\$ 148,898	\$ -
Loans held for sale	5,253	-	5,253	-
Derivative assets:				
Customer-initiated derivatives	3,468	-	3,468	-
Forward contracts related to mortgage loans to be delivered for sale	41	-	41	-
Interest rate lock commitments	41	-	41	-
Total assets at fair value	<u>\$ 195,116</u>	<u>\$ 37,416</u>	<u>\$ 157,701</u>	<u>\$ -</u>
Derivative liabilities:				
Customer-initiated derivatives	3,468	-	3,468	-
Forward contracts related to mortgage loans to be delivered	4	-	4	-
Interest rate lock commitments	12	-	12	-
<i>Total liabilities at fair value</i>	<u>\$ 3,484</u>	<u>\$ -</u>	<u>\$ 3,484</u>	<u>\$ -</u>

The Bank may be required, from time to time, to measure certain assets at fair value on a nonrecurring basis in accordance with GAAP. These adjustments to fair value usually result from application of lower-of-cost-or-market accounting or write-downs of individual assets. The valuation methodologies used to measure these fair value adjustments are described above. For assets measured at fair value on a nonrecurring basis at December 31, the following table provides the level of valuation assumptions used to determine each adjustment and the carrying value of the related individual assets or portfolios at year end.

(in thousands)	Fair Value	Level 1	Level 2	Level 3
<u>2019</u>				
Foreclosed and repossessed assets	\$ 1,440	\$ -	\$ -	\$ 1,440
Impaired loans	31,956	-	-	31,956
	<u>\$ 33,396</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 33,396</u>

(in thousands)	Fair Value	Level 1	Level 2	Level 3
<u>2018</u>				
Foreclosed and repossessed assets	\$ 2,103	\$ -	\$ -	\$ 2,103
Impaired loans	36,654	-	-	36,654
	<u>\$ 38,757</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 38,757</u>

## NOTE 21 – ALPINE BANKS OF COLORADO (Parent Company Only)

The following are the condensed financial statements of the Parent Company.

<b>Condensed Statements of Financial Condition</b> (in thousands)	December 31,		
	2019	2018	
<b>Assets</b>			
Cash and interest earning deposits	\$ 12,654	\$ 12,746	
Investment securities	549	107	
Investment in subsidiary bank	397,005	352,142	
Other assets	1,796	1,353	
<i>Total Assets</i>	<u>412,004</u>	<u>366,348</u>	
<b>Liabilities and Stockholders' Equity</b>			
Subordinated debentures	69,179	69,179	
Other liabilities	383	414	
Total stockholders' equity	342,442	296,755	
<i>Total Liabilities and Stockholders' Equity</i>	<u>\$ 412,004</u>	<u>\$ 366,348</u>	
<b>Condensed Statements of Income</b> (in thousands)	Years Ended December 31,		
	2019	2018	2017
<b>Interest Income</b>			
Interest and dividends on interest earning deposits and other assets	\$ 99	\$ 80	\$ 46
<i>Total Interest Income</i>	<u>99</u>	<u>80</u>	<u>46</u>
<b>Interest Expense</b>			
Subordinated debentures	3,653	3,495	2,949
<i>Total Interest Expense</i>	<u>3,653</u>	<u>3,495</u>	<u>2,949</u>
<i>Net Interest Expense</i>	<u>(3,554)</u>	<u>(3,415)</u>	<u>(2,903)</u>
<b>Non-interest Income</b>			
Dividends from subsidiary bank	17,900	16,900	15,600
Equity in undistributed income of subsidiary bank	42,862	40,227	21,000
Other income	120	501	103
<i>Total Non-interest Income</i>	<u>60,882</u>	<u>57,628</u>	<u>36,703</u>
<b>Non-interest Expense</b>			
Professional services	130	40	32
Other expense	17	21	115
<i>Total Non-interest Expense</i>	<u>147</u>	<u>63</u>	<u>147</u>
<i>Net Income Before Income Taxes</i>	<u>57,181</u>	<u>54,150</u>	<u>33,653</u>
<b>Income Tax (Benefit) / Expense</b>	<u>(827)</u>	<u>(699)</u>	<u>18</u>
<i>Net Income</i>	<u>\$ 58,008</u>	<u>\$ 54,851</u>	<u>\$ 33,635</u>

<b>Condensed Statements of Cash Flows</b> (in thousands)	Years Ended December 31,		
	2019	2018	2017
<b>Cash flows from operating activities:</b>			
Net income	\$ 58,008	\$ 54,851	\$ 33,634
Adjustments to reconcile net income to net cash provided operating activities:			
Equity in undistributed income of subsidiary bank	(42,862)	(40,227)	(21,000)
Deferred income taxes (benefits)	93	-	1,448
Net change in other assets and liabilities	(452)	56	(2,108)
Net cash (used in) provided by operating activities	14,787	14,680	11,974
<b>Cash flows from investing activities:</b>			
Other, net	(40)	450	-
Net cash (used in) provided by financing activities	(40)	450	-
<b>Cash flows from financing activities:</b>			
Common stock cash dividends paid	(12,282)	(11,412)	(10,587)
Repurchase of common stock	(2,557)	(3,480)	(171)
Net cash (used in) provided by financing activities	(14,839)	(14,892)	(10,758)
Net increase in cash and cash equivalents	(92)	238	1,216
Cash and cash equivalents at the beginning of year	12,746	12,508	11,292
Cash and cash equivalents at the end of year	\$ 12,654	\$ 12,746	\$ 12,508

## NOTE 22 – SUBSEQUENT EVENTS

The Bank has evaluated subsequent events through February 1, 2020, the date at which the consolidated financial statements were available to be issued, and determined that no events have occurred would require disclosure.